

**REPORT BY THE CONSUMPTION TAX  
TECHNICAL ADVISORY GROUP (TAG)**

**December 2000**

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## REPORT BY THE CONSUMPTION TAX TECHNICAL ADVISORY GROUP (TAG)

### **EXECUTIVE SUMMARY: REVIEW OF WORK AND PRINCIPAL OUTPUTS AND CONCLUSIONS**

#### *Overview and background*

##### *Composition of the Consumption Tax TAG*

1. The members of the Consumption Tax Technical Advisory Group (CT TAG) were drawn from countries with a broad geographical spread and the government representatives included non-OECD members. The business members were drawn from a wide range of industries. The role of the CT TAG was to work through its mandate (see Annex I), so supporting the work of Working Party No. 9 on Consumption Taxes (WP9) in fleshing out the consumption tax aspects of the Taxation Framework Conditions endorsed at the Ottawa Ministerial meeting held in October 1998 (the “Ottawa Framework”).

##### *Working methods*

2. From an early stage, it was agreed by both the business and government members of the CT TAG (and by the Working Party No. 9 Sub-group on Electronic Commerce – “Sub-group”) that the TAG could best support the process as a whole (particularly in advising the Sub-group) if it functioned predominantly as a mechanism for identifying business concerns and priorities. In practice, this approach facilitated an iterative dialogue (involving both the exchange of papers, and joint meetings) between the TAG (broadly representing a business perspective) and the Sub-group. In this mode, the TAG was able more readily to offer responses to papers from the Sub-group, as well as generate its own ideas, which directly reflected business thinking. The Sub-group found this a productive way to get feedback and input from the TAG, and has reflected such input in the WP9 Report to the Committee on Fiscal Affairs (CFA) (identifying clearly business concerns, priorities, points of agreement, and differences).

3. Given this working method employed by the TAG, the terms of this report inevitably focus on the papers which were produced by the business members, and which reflect, principally although by no means exclusively, their perspective. In many instances the process has helpfully identified a good deal of common ground between business and government (as identified below, and in the WP9 Report to the CFA).

### *Progress of work*

4. The CT TAG met on five occasions between April 1999 and October 2000. The early meetings were spent in getting acquainted and focusing in on the tasks which were necessary to fulfil the mandate. With the agreement and support of the government members, the business members basically set themselves various tasks, in the form of drafting papers, and divided into “mini-groups” to achieve this. The tasks evolved somewhat over the period but four main issues were studied and papers on these were presented to the full CT TAG and then to the Sub-Group. The CT TAG was invited on three occasions to meet with the Sub-Group to review and debate the papers and issues concerned. These invitations and the open-minded approach which lay behind them were welcomed by the business members and the free debate generated was regarded as very constructive. The issues identified through the working process of the CT TAG are described more fully below and have been reflected by the Sub-group at various points in the Report it has prepared on behalf of WP9 for submission to the CFA (the “WP9 Report”). The business members of the CT TAG note this point and are encouraged that their contribution to the process is viewed as constructive and helpful.

### *Issues covered and recommendations*

#### *1) Place of consumption*

*See Annex II*

5. The Ottawa Framework states as a broad principle that taxation should take place in the jurisdiction where consumption takes place. In its deliberations, the entire CT TAG identified early on that it would not be possible to identify or trace every individual event of consumption and that it would be necessary to identify a less precise, but more practical and workable test by which to identify which country’s consumption tax is due on a particular transaction. The business members came to the conclusion, later supported by the government members, that the most practical solution is to look at the customer’s usual place of residence. This latter conclusion is reflected in the WP9 Report. This led to consideration of what constitutes adequate verification of usual place of residence. Government members expressed concern that it would be difficult to accept customer-provided information without a means of verifying that the information provided was correct. Business members felt strongly that companies should be able to rely on the best information available at the time of a transaction, noting that verification requirements that delayed completion of a transaction or resulted in substantial costs unrelated to the normal course of business would undermine the growth of e-commerce and be inconsistent with the principles adopted at Ottawa.

6. Business members suggested that the quality of information available at the time of a transaction is expected to evolve over time. In the short term, businesses might have to rely on such factors as customer attestation, credit card billing address as provided by the customer, the language of the digitised goods or services being delivered, or the target market for digitised goods or services. In the longer term, much more robust verification options may be available including options that enable the identification of the income tax residence of the purchaser.

7. Given that the Ottawa Framework is intended to prevent tax issues being a barrier to the growth of electronic commerce, it is hoped that a practical approach will be adopted with real-time verification only being sought by governments when the mechanisms exist for this to be done. The TAG welcomes the recognition in the WP9 Report that further work is needed on verification.

8. How consumption tax is collected on electronic commerce is clearly a key issue and both the business members of the CT TAG and the government members of the Sub-Group spent considerable amounts of time working on this topic. Both groups acknowledged that there is no “easy” solution to be found, at least for B2C on-line transactions. It was agreed as common ground that a “self-assessment” or “reverse charge” mechanism is a logical way for tax on business-to-business (“B2B”) transactions to be collected. With respect to business-to-consumer transactions (“B2C”), the following models and potentially relevant technological developments were examined, and the key points are noted under each point:

(a) *Consumer self-assessment, both business and non-business*

The CT TAG agreed that self-assessment for business customers is a simple, highly-desirable mechanism for taxing business to business transactions. With respect to private customer transactions, it was agreed that consumer self-assessment is not likely to be an effective tax compliance mechanism in the near term. However, the business members recommended that the self-assessment model continue to be reviewed in light of emerging technologies and changing business models. Due to technological changes driven by other factors (such as privacy, fraud and piracy prevention) consumer self-assessment might in the future become a viable means of collecting consumption tax and an open mind should be kept as to its potential feasibility.

(b) *Registration of non-resident suppliers*

The CT TAG agreed that for this model international co-operation would be necessary to make compliance by vendors enforceable. Until such mechanisms are available the business members pointed out that registration and compliance procedures should be as straightforward and simple as possible – see also the Simplified Interim Approach (“SIA”) section 4 below. In particular, use of expensive and cumbersome fiscal representative procedures should not be enforced. The business members also noted that, in time, a registration model might be combined with “trusted third party” models which are in course of development. Options should be kept open for vendors to use such models in due course.

(c) *Tax at source and transfer*

The CT TAG agreed that the tax at source and transfer model would entail an extremely high level of international co-operation between tax authorities and as such might not only be unrealistic in the near term but difficult to achieve in the long term as well. The most significant limitation of this discussion is that it focuses on a relatively narrow way in which this type of approach may work and, thus, may perhaps prematurely conclude that there is little potential here.

(d) *Withholding by third parties (such as financial institutions)*

In response to the publication of Technology TAG paper, a number of financial services companies (particularly credit card companies) have submitted papers to the OECD, identifying a number of significant issues and concerns. We welcome this information and to the extent points discussed below are contrary to points made in these submissions, we would defer to those other papers. We agree with the Technology TAG’s conclusion that the suggested framework is unrealistic.

3) *Summary of current consumption tax barriers to the development of electronic commerce*

*See Annex IV*

9. The business members noted the principles stated in the Ottawa Framework that taxes applied to e-commerce should be efficient, certain and simple. However, in practice, consumption tax rules as they apply to conventional business do not have these characteristics and it was thought by the business members that complexities in existing rules may be a barrier to both conventional and electronic commerce. A small group of CT TAG members therefore drafted a paper concerning these barriers and some general recommendations for simplification. The business members of the TAG welcome the recognition in the WP9 Report of the important role of simplification, and encourage governments to address selected urgent issues such as, for example, electronic invoicing and reporting, simplification of representation procedures, more efficient payment and refund procedures, as a priority.

4) *Simplified interim approach (“SIA”)*

*See Annex V*

10. Given the difficulties of identifying a workable collection option (see section 2 above), the business members put forward, firstly by presentation, and secondly on paper, the suggestion of a simplified tax compliance system which would hopefully encourage vendors not established in a particular country to collect and remit tax. This was seen as an interim measure, only operating until one or more of the collection options described above, or a new option, developed into a feasible system. The potential value of this approach is recognised in the WP9 Report, and business members of the TAG strongly recommend that governments give this idea further detailed consideration.

11. The SIA focuses on the need to simplify all aspects of tax compliance for non-established sellers, including registration, identification of turnover and calculation of tax, electronic submission of returns and audit processes. Access to relevant information and provision of information regarding changes should be made available on-line.

12. The thrust of the SIA is that VAT compliance should be so simple that non-established vendors would be thereby encouraged to register.

***Next steps and future work***

13. As noted above, the members of the CT TAG consider that the TAG process has been helpful and constructive in progressing the work identified in the Ottawa Framework. It is hoped that the TAG will be retained as a mechanism for incorporating joint government and business input into the important process of finalising the policy of how consumption taxes should be applied to electronic commerce. In this respect the CT TAG has identified possible further work areas as follows:

1) *Place of consumption*

Work to expand and refine the list of “proxies” which may be used to identify the permanent address or usual place of residence of a customer. It is possible that this work may benefit from being carried out in conjunction with Technology TAG members.

2) *Work to assess potential tax collection options being developed*

The CT TAG should continue to assess all forthcoming developments in this area, for example see the examples set out in Annex III.

3) *Current consumption tax barriers*

Further work between government and business members to develop the suggestions for simplification and to focus on these which have the most potential benefit for business and the maximum possibility of being adopted globally.

4) *Simplified interim approach*

Further work to expand and develop the initial ideas into a comprehensive model.

## **Conclusions**

14. The CT TAG agrees with the conclusions in the WP9 Report as follows:

*A) Guidelines on the definition of the place of consumption*

- i) That the application of the Taxation Framework Conditions to international trade in services and intangible property can best be achieved by: (1) defining the principle of taxation in the place of consumption more clearly, and (2) identifying collection mechanisms that can support the practical operation of that principle.
- ii) That this principle should be expressed in the form of OECD “Guidelines on the Definition of the Place of Consumption for Consumption Taxation of Cross-Border Services and Intangible Property”.
- iii) That such Guidelines should define the place of consumption:
  - a) For business-to-business (B2B) transactions, by reference to the jurisdiction in which the recipient has located its business presence; and
  - b) For business-to-consumer (B2C) transactions, by reference to the recipient’s usual jurisdiction of residence. And that further work is required on appropriate means of verifying the latter.

*B) Recommendations on collection mechanism options*

- iv) That the most viable collection mechanisms to support the practical application of such Guidelines lie:
  - a) In a reverse charge or a self-assessment mechanism for B2B transactions; and
  - b) In the short term (pending adoption of technology-facilitated options), in some form of registration-based mechanism for B2C transactions with specific efforts being made to promote simplified approaches to registration of non-resident suppliers.
- v) That in the medium term, particularly in the context of collection mechanisms for B2C transactions, technology-based options offer genuine potential and merit more detailed examination in active co-operation with business.

*C) Related issues*

- vi) That the growth in cross-border e-commerce presents new international challenges for indirect tax authorities, and so underlines the need for substantially greater levels of international administrative co-operation.
- vii) That the dialogue with the business community and non-members, as part of the post-Ottawa process should continue as part of ongoing work on selected issues.

- viii) That simplification has important role to play in addressing business concerns, minimising compliance costs and reducing administrative costs, and that further work is necessary to assess and progress various ideas and options.

***Business members' summary comments***

15. The business members feel strongly that the simpler the solution, the greater the level of compliance would be and that future requirements should leverage the development of commercial business models. E-commerce models are evolving, suggesting that business and governments should work together to review opportunities to use new developments to increase the effectiveness and robustness of tax collection mechanisms. Business members feel they have a helpful role to play in this process.

**ANNEX I:  
MANDATE AND COMPOSITION OF THE TAG**

**Topics for consideration by the Consumption Tax TAG**

**1. *Tax collection***

- To advise on practical experience in tax collection mechanisms in the context of electronic commerce transactions.
- To advise on any obstacles that existing tax collection mechanisms present to electronic commerce transactions, and to suggest feasible and effective solutions or options to address those obstacles.
- To advise on the channels and mechanisms used commercially to assist in and secure collection of payment from electronic commerce transactions, with a view towards considering whether such mechanisms may be instructive for improving or simplifying tax collection.
- To advise on experience with mechanisms used commercially to identify or to determine characteristics of the customer in an electronic commerce transaction, in particular how to determine whether the customer is an individual consumer, a business, or a public or other non-business entity for consumption tax purposes.
- To advise on practical experience in the use of the reverse charge or similar mechanisms.
- To advise on any obstacles to the use of the reverse charge or similar mechanisms in the context of the transmission of digitised information, and to suggest feasible solutions or options to address any such obstacles.

**2. *Tax compliance***

- To advise on areas within tax compliance that are most in need of simplification, and to suggest feasible options to help accomplish simplification, particularly (but not limited to) the areas of:
  - electronic invoicing and invoicing standards
  - notification and registration
  - tax declaration
  - payment mechanisms
- To advise on commercial development in consumption tax compliance software, from the perspective of commercial users of such software.
- To advise on the development of the agent or intermediary sector, and on the possible roles of trusted third parties, to help business meet tax obligations.

### 3. *Tax policy issues*

- To advise on business concerns and views regarding how to achieve internationally compatible definitions of place of consumption and of services and intangible property.
- To advise on the types of services and intangible property for which greater clarity is needed as regards determining the place of consumption.
- To advise on business views regarding the technical feasibility, ease of administration, and other commercial aspects of policy proposals that the sub-group submits to the TAG for its consideration.

### **Composition of the TAG**

The following people participated in the activities of the TAG and attended one or more of its meetings.

<b>Full Name</b>	<b>Company/Organisation</b>
Mr. Satoshi WATANABE ( <i>Government Co-Chair of the TAG</i> )	Institute of Economic Research, Hitotsubashi University, Japan
Ms. Christine SANDERSON ( <i>Business Co-Chair of the TAG</i> )	PriceWaterhouseCoopers, United Kingdom
<b>Government representatives</b>	
Mr. Michael HARDY	Australian Tax Office
Mr. Eimon UEDA	Ministry of Finance, Japan
Mr. Robert BOOGAARD	Ministry of Finance, Netherlands
Mr. David HOLMES	HM Customs and Excise, United Kingdom
Mr. Jeffrey FRIEDMAN	United States Treasury
Mr. Michael MUNDACA	United States Treasury
Mr. Arthur KERRIGAN	European Commission
Mr. Geoff TRUEMAN	European Commission
Ms. Andréa LEMGRUBER VIOL	Brazilian Federal Tax Administration
Ms. Huey-Min CHIA-TERN	Inland Revenue Authority of Singapore
<b>Business representatives</b>	
Ms. Ellen K. FISHBEIN	America Online, Inc., United States
Mr. Michael LIDDICK	America Online, Inc., United States
Mr. Markus FOELLMI	UBS AG, Switzerland
Mr. Hiroshi KADOTA	Keidanren, Japan
Ms. Karen M. MYERS	Electronic Data Systems Corporation, United States
Ms. Nancy PERKS	Microsoft Corporation, United States
Mr. Glen PYE	Nortel Networks, Canada
Mr. Graeme ROSS	KPMG, United Kingdom
Mr. Gabriel RUMO	Swisscom AG, Switzerland
Ms. Judy SCARABELLO	AT&T, United States
Mr. Rien WIJTMANS	ABN AMRO Bank N.V., Netherlands
Mr. Henk WILDEBOER	Philips International, Netherlands

**ANNEX II:  
PAPER ON PLACE OF CONSUMPTION PRINCIPLE**

**RESPONSE TO JANUARY 2000 PLACE OF CONSUMPTION PAPER PREPARED  
BY WORKING PARTY NO. 9 SUB-GROUP ON ELECTRONIC COMMERCE**

*[Submitted to the WP9 Sub-group by the Business Members of the Consumption Tax TAG, April 2000]*

**General**

1. The place of consumption paper<sup>1</sup> drafted and circulated in January 2000 by Working Party No. 9 Sub-group on Electronic Commerce (the “Sub-group”) reflects significant effort and determination to understand the complex issues involved in taxing electronic commerce. We appreciate the Sub-group’s thoughtfulness and diligence in attempting to identify and resolve the challenges that face suppliers as well as tax administrators regarding these issues.

2. The Sub-group makes many observations in its paper with which we agree. There are, however, several important issues that we believe warrant further discussion. There are also several additional factors that must be considered as various options are weighed. These are set forth below.

**Points of agreement**

3. There are a number of general concepts with which we strongly agree. One in particular, in the Introduction of the Sub-group’s paper, deserves specific mention. The paper states: “Taxation at the place of consumption will, from an international point of view, lead to an *equal burden of consumption taxes on the same products in the same market.*” (page 3, section 2) (emphasis added). This concept, which could also be referred to as the principle of neutrality, is extremely important to all parties in this tax debate. We believe that, in the case of business-to-private transactions, the concept of treating the customer’s normal residence as the place of supply represents a significant step in achieving neutrality between e-commerce transactions and traditional forms of transactions.

4. It is critical that we identify tax policies that do not treat goods or services sold over the Internet any differently than goods or services sold through traditional means. If the tax policies that are implemented for electronic commerce fail to treat the sale of “on-line” goods and services the same as “offline” goods and services, they will affect the buying behaviour of consumers, causing them to favour one sales distribution channel over another – a result which goes against the well-established tax policy principle of neutrality. In other words, tax administrators should consider all issues that create situations in

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1. This paper, to which the present document refers was a working draft shared with the Consumption Tax TAG but not made publicly available. The salient features of the paper, however, feature in the Working Party No. 9 Report to the Committee on Fiscal Affairs (see <<http://www.oecd.org/daf/fa> for a link to the “Report by the Committee’s Working Party No. 9 on Consumption Taxes: Consumption Tax Aspects of Electronic Commerce”).

which digital supplies are taxed differently from traditional supplies that are essentially similar. In some cases, additional steps may be required to achieve neutrality.

5. We also generally agree with the options suggested for the treatment of business-to-business transactions and business-to-non-business transactions, which appear to be workable and well grounded in existing practices. Where the customer has only one location, the supplier should look to the customer's location as the applicable taxing jurisdiction.

6. If the customer has more than one location, the supplier should be permitted to rely solely on the terms of the contract to determine the applicable taxing jurisdiction. When one multinational company deals with another multinational company on a global contract, that contract will generally specify which legal entities are making supplies and which legal entities are acquiring supplies. The terms of the contract should be respected for collecting tax. For example, the contract might state that one supplier will sell all goods and services to one customer. In this case, the supplier would issue a single invoice to the customer entity, and the appropriate taxing jurisdiction would be the location of that customer. This rule would apply regardless of whether the customer entity subsequently distributes such goods and services to affiliates through invoiced, inter-company sales.

7. Alternatively, the contract may specify that a number of supplier affiliates will make separate supplies to various customer affiliates. Each supplier affiliate making supplies would issue a separate invoice to the appropriate affiliate of the customer group. In this scenario, each invoice between supplier and customer should be analysed separately, and the appropriate taxing jurisdiction would be the location of the customer on each invoice.

8. The point in each of these examples is that companies should have the ability to determine the ways in which they choose to do business with each other, and VAT rules and invoicing requirements should permit companies to appropriately invoice the way in which they choose to conclude the transaction.

9. With respect to business-to-private transactions, the Sub-group's suggestion that governments should look to the customer's permanent address or usual place of residence as the place of consumption is a very practical rule for providers to follow. The most practical way to apply this rule is to allow the service provider to rely, in the first place, on the customer's address, as provided by the customer during the course of the transaction, without having to inquire further into whether the address is the customer's permanent address or usual place of residence.

10. Suppliers should be able to rely on the customer's address for computing tax on all transactions, regardless of whether the supply involves goods, services, tangible property or intangibles. It should be recognised, however, that there are significant limitations to this approach for transactions involving intangible goods, such as downloaded music, books or videos. During these transactions, a customer may not be required to provide any personal information, because the customer's location is irrelevant for purposes of transferring the good to him or her.

11. Given consumer concerns and government protections relating to privacy issues, a supplier should not be required to ask for information during the course of a transaction, which a consumer might perceive as creating issues relating to personal privacy. For example, a supplier should not be required to ask for a national health service number, Social Security number, or driver's license number; asking for such personal information is likely to dissuade consumers from concluding the transaction. Research has been conducted that indicates that many customers will abandon a transaction if they are required to provide more information than is necessary to complete the transaction.

12. Usually, a supplier is in the best position to know what information can be requested of a customer without triggering concerns of privacy. In some cases, suppliers may be able to collect information relating to a high level geography of a customer's address (*i.e.* country of residence). In other instances, even this request may be viewed as inappropriate.

13. If a supplier chooses to request information regarding the customer's address or place of normal residence when such information is otherwise not required to conclude the transaction, the supplier must be able to rely on that information without further verification to compute the tax on the transaction. Creating such a "safe harbour" would also encourage more suppliers to voluntarily ask customers for this information even if such information is not ordinarily requested or required during the transaction.

14. If country of residence information is not routinely collected and the supplier believes requesting such information would be inappropriate, another alternative would be to permit suppliers to rely on a reasonable "sourcing proxy" based on the supplier's business model. For example, if a supplier has a web site where consumers can purchase German books in a digitised format that can be downloaded directly from the web site to their computers and the supplier focuses his marketing effort on German consumers (*e.g.* the web site is written only in the German language), the reasonable "sourcing proxy" would be Germany. Therefore, the supplier would charge German VAT on all transactions concluded at that web site. If this alternative is permitted, however, it is important that a supplier's good faith efforts in identifying a "sourcing proxy" be respected.

15. There are also other possible alternatives which merit consideration: First, customers themselves could be held responsible for sourcing, assessing and remitting such taxes to the appropriate taxing authorities. Second, the supplier could be permitted to impose a specific flat rate on such transactions. The supplier could then remit taxes from such transactions to one taxing authority that would distribute the funds among all participating countries. Third, it may be possible to develop a system that allows the supplier to compute the tax based on the country in which the credit card used for purchase was issued. The viability of this option, however, depends on whether credit card companies are both willing and able to provide this information. If this option is desirable, it is recommended that credit card company representatives be invited to participate in this dialog to determine the availability of this information. Finally, if none of these alternatives is desirable, practical or available, the only alternative may be to forego taxing and collecting on such transactions until such time as a technological solution evolves that permits identification of the source of the transaction without eliciting such information from the customer.

16. It may well be worthwhile to initiate a study to determine which, if any, of these options is most promising in the long term. In the short term, however, it would seem to be in the mutual best interests of governments and businesses to permit sellers to make the best good faith effort based on information that is currently available during the course of the transaction.

17. Finally, with respect to any of the alternatives set forth above, the quality of information available may vary considerably depending on the type and size of the transaction. Recognising that the administrative burden of tracking small transactions, where information accuracy may be questionable and tax revenues are not significant, *de minimus* thresholds should be established so that relatively insignificant transactions (those involving less than a certain total or per item value) would be exempted entirely from consumption taxes.

## **Other points for discussion**

18. With respect to business-to-private transactions, the Sub-group suggests (in sections 7.5 and 8.13) the option that a “two out of three” test could be adopted to identify the place of consumption (the “three” being the country to which the service is delivered, the country to which the customer’s bill is sent and the country which issues the credit card used for payment). The “two out of three” option would create, rather than reduce, administrative burdens. Further, multiple tests are not practical in an environment in which transactions are concluded instantaneously and are likely to result in less, rather than greater certainty for suppliers.

19. Another point that warrants further discussion involves the distinction between “tangible services where the participants need to be in the same location, and intangible services where the participants are remote.” (page 10, section 9.5). It seems that a simple solution to this problem – and one that would foster the concept of tax neutrality and fairness – would be to allow the supplier to rely on one rule—based on the location of the consumer. In the case of remote sales, the consumer’s location would be presumed to be the consumer’s normal address.

## **Conclusion**

20. The Sub-group’s paper makes significant strides in highlighting the issues in identifying the place of consumption. In determining the appropriate resolutions of these issues, we urge the Sub-group to focus on simplicity and neutrality – both with respect to the tax treatment of “on-line” and “off-line” goods and with respect to the collection burdens of “on-line” and “off-line” suppliers.

21. In the short term, governments should expect businesses to make the best good faith effort to identify the place of consumption based upon data available during the transaction. Where data is unavailable, there should be a shift of responsibility (either for providing information or for tax collection) to the customer. Reasonable *de minimus* rules should be implemented to further balance expected tax collections with administrative costs imposed by the tax collection requirements.

22. Longer term approaches should take into consideration developments in technology, electronic payment systems (with the input and consent of payment system representatives) and trends in business models to leverage these developments to continually simplify the solution for identifying the location of the consumer’s normal residence.

**ANNEX III:  
PAPER ON TAX COLLECTION MECHANISM OPTIONS**

**RESPONSE TO THE JANUARY 2000 TAX COLLECTION MECHANISMS PAPER  
PREPARED BY WORKING PARTY NO. 9 SUB-GROUP ON ELECTRONIC COMMERCE**

*[Submitted to the WP9 Sub-group by the Business Members of the Consumption Tax TAG,  
November 2000]*

**Introduction**

1. The Working Party No. 9 Sub-group on Electronic Commerce paper entitled, *Electronic Commerce—Tax Collection Mechanisms* (WP9 Sub-group Paper or “Paper”)<sup>2</sup> is an accurate and thoughtful analysis. The Paper examines the administrative burden, jurisdiction, enforcement and verification issues arising in the context of the most problematic area of e-commerce – business-to-consumer (B2C) transactions which can be entirely digitally fulfilled and do not involve physical shipments. The focus on such a narrow aspect of e-commerce is understandable given the viewed adequacy of existing mechanisms (*i.e.* business self-assessment, and border clearance processes) to create a compliance solution for other aspects of e-commerce. Focusing on such a narrow segment of commerce, however, may have unintended negative consequences on the broader category of cross-border commerce.

2. We feel that focusing on this narrow aspect of e-commerce from a compliance perspective is a lost opportunity. A broader examination might provide the opportunity to devise a more robust taxation system which can more adequately address the increase in cross-border-trade and potentially offer solutions which are much more scalable and less costly for all parties involved.

3. To illustrate, the existing border clearance process provides a compliance solution for governments, but does little if anything to facilitate the growth of cross-border transactions and particularly low value transactions. Businesses and consumers both will continue to be reluctant to engage in transactions in which the final cost of the transaction remains uncertain due to the potential applicability of duties and consumption taxes. Specifically, business will be reluctant to trade internationally if uncertainty about the fully landed costs of products results in a high level of returns or if product delivery dates remain uncertain due to the length of time required to clear goods.

4. From the business perspective, the primary issue is how best to facilitate increasing international or cross-border trade, and not simply how to trade in electronically delivered goods and services. Business would prefer to see tax solutions focused on all areas of international trade not just those limited to digitally deliverable goods and services.

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2. This paper, to which the present document refers was a working draft shared with the Consumption Tax TAG but not made publicly available. The salient features of the paper, however, feature in the Working Party No. 9 Report to the Committee on Fiscal Affairs (see <<http://www.oecd.org/daf/fa> for a link to the “Report by the Committee’s Working Party No. 9 on Consumption Taxes: Consumption Tax Aspects of Electronic Commerce”).

5. Another limitation of the paper is that it addresses only those compliance models that center all responsibility and liability for compliance on a single party. This is somewhat unusual given that existing models of international or cross-border trade currently split the responsibility for tax compliance among a number of parties including government officials, freight forwarders, and suppliers. The paper assumes that, as is the case with domestic transactions, a single party (the supplier) is in the best position to manage all aspects of consumption tax compliance. We suggest that potential collection options should be expanded to include consideration of options, which assign responsibility for different aspects of compliance to the parties that are best capable of performing a specific function or of providing specific information. In the case of B2C transactions, a customer option should be included.

## **Business members' comments on the Tax Collection Mechanisms Paper**

### *Self-assessment*

6. The business members agree that self-assessment is the preferred option for business-to-business (B2B) transactions. We also agree with the point that consumer self-assessment is not likely to be an effective tax compliance mechanism in the near term, however, we recommend that the self-assessment model continue to be reviewed in light of emerging technologies and changing business models. Consumer self-assessment might become a viable means of collecting consumption tax in the future.

### *Additional observations*

7. One important potential benefit of consumer-based compliance models is that the taxing authority has jurisdiction over its consumers. The primary benefit is that such an approach increases the likelihood that tax is ultimately collected from the party that is meant to bear the tax. At present, use tax collection methods and consumer self-assessment leave much to be desired, however, the strength of the connection between the jurisdiction and the consumer make this an area that warrants further examination. It is premature to rule out the potential for other consumer-based collection mechanisms at this stage.

8. The infrastructure that will emerge to support e-commerce will include a number of different elements, which will evolve to meet specific business or customer needs. At present, much of the existing infrastructure was created for traditional forms of commerce and does not necessarily reflect the structures that will eventually be designed to deal with e-commerce specifically. For example, while credit cards are frequently used to make payments with regard to transactions over the Internet, credit cards were not specifically designed to deal with e-commerce. Future payment system products are likely to include features that better manage e-commerce transactions including a more effective way to deal with fraud, increased protection of consumer privacy, etc. New features will continue to emerge to meet market demand.

9. While it is impossible to predict what these new features will be, we believe it is useful to outline one possible approach to how consumer-based liability models might work in the future. The mechanism outlined below is purely hypothetical. The goal is to define how such an approach might be made “automatic,” enforceable, and effective.

10. In the future, smart cards may be developed for a variety of purposes, and governments may leverage or exploit the use of such technology to replace drivers' licenses, passports, etc. The smart card could also be designed to provide details on a consumer's taxing jurisdiction and include a tax account number that could be used by the consumer for purposes of determining tax. Future smart card programs

might be capable of recording the details of the cardholder's on-line transactions and the amount of consumption tax due.

11. Merchants could use the details programmed on the smart card for determining that tax was not required to be collected and to maintain records of transactions paid by tax account number to facilitate reporting. The consumer could arrange for up-front consumption tax payments through his payment system provider.

12. The smart card could be used by the consumer to file a periodic summary tax return of total on-line purchases and total consumption tax due. The consumer could automatically file the return by going to the on-line tax web site and inserting the smart card into a card reader. While the consumer would receive a record of all transactions, privacy concerns would most likely prevent the reporting of transaction details to the government. The consumer should have some assurance that only total amounts, not transaction details, would be available to tax authorities.

13. For the system to be effective, it would be necessary for suppliers making supplies into a jurisdiction to obtain the tax account number from the consumer to complete the transaction. Liability for under-collected tax would revert to the supplier if the supplier chose to complete the transaction without a properly programmed smart card that included the necessary tax account number. If the smart card data were properly used by the supplier to compute and remit tax, then any shortfall would be collected by the government directly from the consumer (*e.g.* by redirection of tax refunds or by invoice).

14. It is expected that most suppliers would be diligent about correctly computing the tax to avoid major consumer satisfaction problems. As with any system, however, it is possible that some suppliers would not be as conscientious, requiring some type of supplier enforcement program to discourage suppliers that refused to utilise the infrastructure appropriately.

15. We realise that international co-operation would be required for this approach to work because governments would need to have compatible systems in place.

16. This example is only provided as a model. It also indicates that any solution will require at least some degree of international co-operation in order to be effective, and it demonstrates that any consumer-based system must be extremely automatic and easy for the customer to use.

### ***Seller registration***

17. The WP9 Sub-group Paper seems to imply that seller registration would not be required in the context of B2B transactions. If we understand this correctly this is certainly a strong point of agreement. This point does not, however, address situations where countries do not have a self-assessment or use tax system. The Paper also makes the reasonable assessment that the success with seller registration in the telecommunications industry experienced in the European Union is not necessarily a reliable indication of potential success of a similar e-commerce model.

18. We agree with the conclusion that seller registration models will require international co-operation in order to establish enforceability.

### ***Liability for collecting tax***

19. It is our understanding that the approach currently favoured by government for the near term is to continue the current model where suppliers are liable for assessing tax on their supplies and for collecting

and remitting the tax due to the relevant national government. To some extent, this may be simplified in trading zones such as the EU where it is possible that a single place of registration may be adopted. The paper drafted by the Technology TAG, *Technological Perspectives on Consumption Tax Collection Models for Cross Border Electronic Commerce Trade* (“Technology TAG Paper”), circulated to the Consumption Tax TAG in April, 2000 also contemplates shifting tax liability to other parties (consumer and/or financial intermediaries). In evaluating the practicalities, we would first like to explore the models that hold the suppliers responsible for assessing, collecting, and remitting tax.

### *Supplier collection models*

#### Supplier point of sale processing

20. One of the most positive aspects of the OECD process is the extent to which our discussions have focused on the practical issues regarding collection models and the related principles. The success of consumption tax systems is largely based on the fact that with conventional commerce, the practical applications integrate reasonably well into the commercial and financial processes of both suppliers and buyers.

#### Practical examples

21. E-commerce is in its relative infancy, which limits the availability of examples that would allow us to evaluate the practical consequences of any of the current proposals. To help with this, we have put together an illustration of the consumption tax decision making, compliance, and reporting process for an e-commerce business involved in selling its products via a web site to customers located in multiple foreign jurisdictions.

#### Multi-channel commerce

22. It is clear that government focus within the Consumption Tax TAG is primarily on digitally distributed products to consumers by suppliers located outside the consumer’s jurisdiction. It is important to recognise, however, that most suppliers that are moving into digital distribution are already providing similar products in hard form. For example, players in the software, music, video and electronic gaming sectors already produce and distribute hard forms of their products. It is highly likely that many of these suppliers will experience a lengthy transition period where products are distributed digitally or in hard form according to the customer’s preferences. Furthermore, it is doubtful that any business will trade only with consumers. We, therefore, need to recognise that supplier systems need to be able to recognise and cope with both hard and soft distribution to both consumers and businesses.

#### Commercial drivers

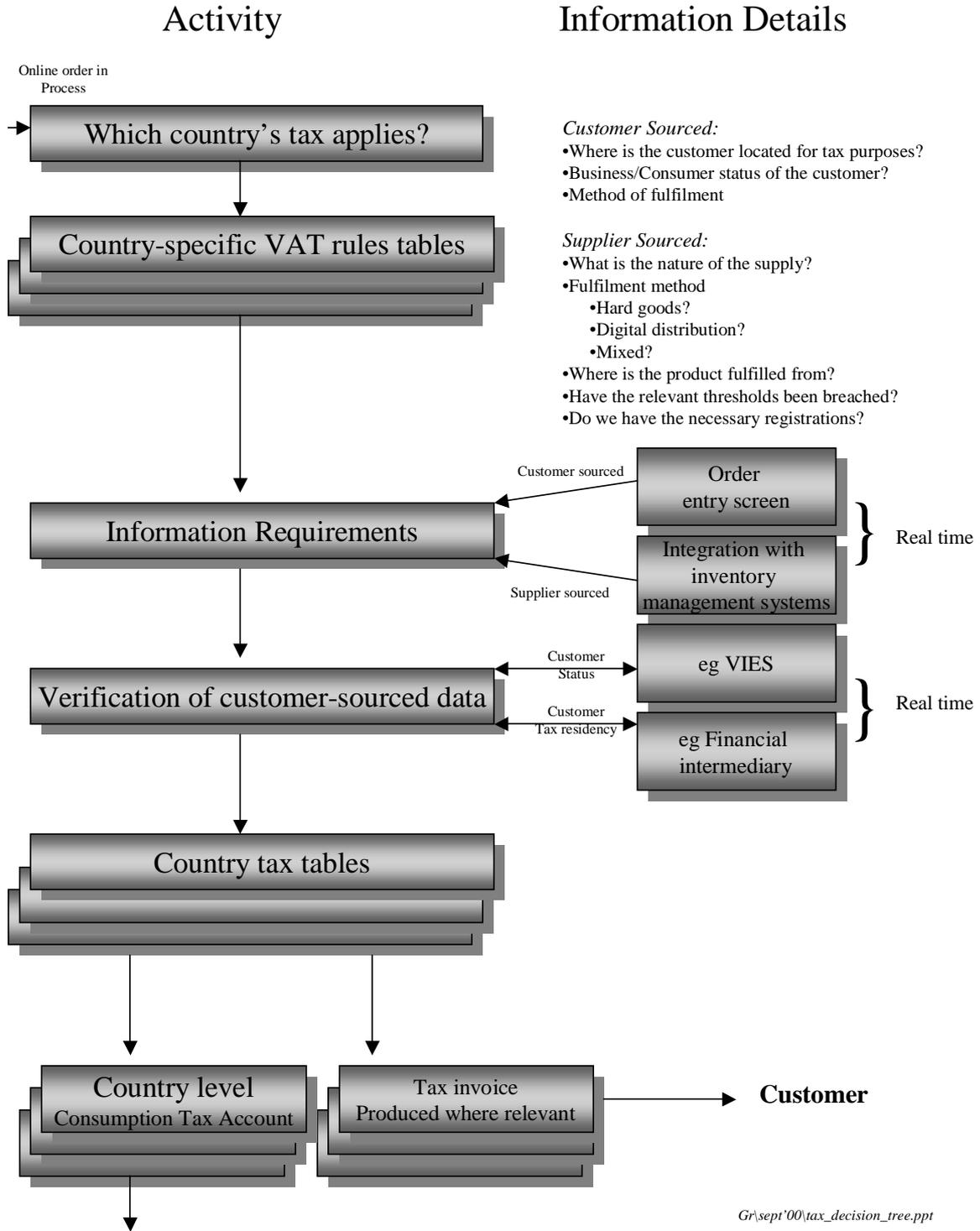
23. The other key factor we need to recognise is that the fundamental driver underpinning the tremendous growth in e-commerce is the cost efficiencies which e-commerce technologies provide to suppliers trading both domestically and internationally. Particularly with digital distribution, there will be no human intervention in the browse-order-pay-fulfil process – this functionality will be fully automated. Accordingly, if taxes are to be applied accurately, it has to be possible for tax rules and processes to be embedded in the suppliers’ browse-order-pay-fulfil processes. Furthermore, the lure of digital distribution turns on customer expectations of instant gratification. The process of applying consumption tax (which

clearly has a significant effect on the price paid) not only has to be capable of full automation, but also has to take place on a real time basis, as the customer's order is processed.

24. With these points in mind, an example of the kind of consumption tax processes a supplier would have to be able to support, together with the necessary information drivers is set out in Figure 1.

**Figure 1. Supplier – tax decision tree**

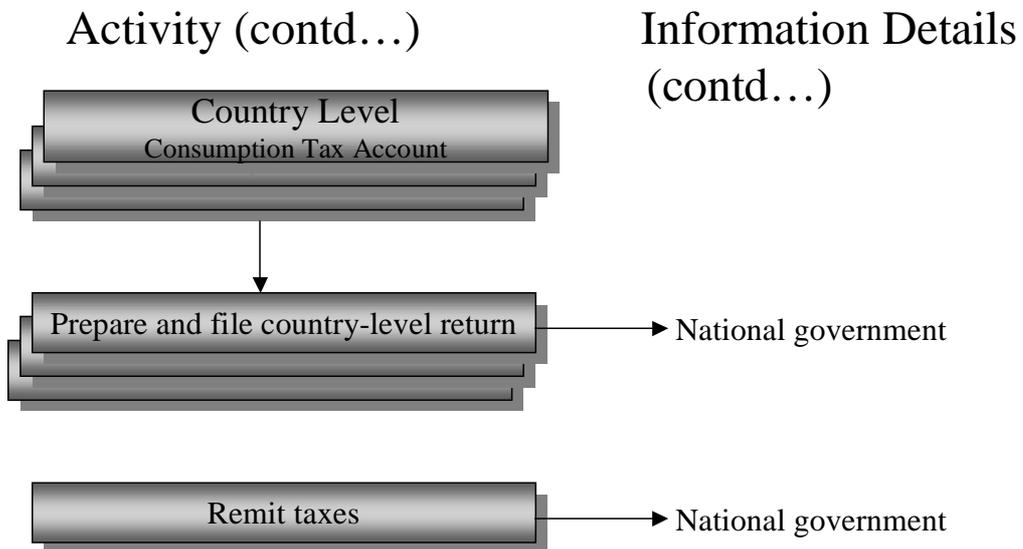
**1) Real Time Processes**



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**Figure 1 (continued).** Supplier – tax decision tree

2) Offline Processes



*Critical success factors*

25. For these processes to operate in practice, there will be a number of requirements, as set out in Table 1.

**Table 1.** Critical success factors

Requirement	Issue
<p><b>Customer disclosure</b></p> <p>Mandatory fields within order screens requiring customers to disclose their address (or at least country of residence) and to provide a tax identification number when they are ordering in a business capacity.</p>	<p>Although both are commercially desirable from a customer profiling perspective, neither requirement is critical to the execution of the transaction.</p>
<p><b>Integration of systems</b></p> <p>The supplier sales order processing system has to be able to integrate with the inventory management system <b>at transaction level</b> in order to determine from where and how the order will be fulfilled. This is critical in establishing the tax treatment in the country from which the product is distributed.</p>	<p>At present, many web sites are hosted by third parties and do not integrate directly with the supplier's sales order processing and inventory management systems. This is not an issue in the simplest case where the supplier always delivers the product in the same form from the same place but is critical for more sophisticated supplier businesses.</p>
<p><b>Country tax rules tables</b></p> <p>Country specific consumption tax rules tables are required for each country where consumption is deemed to take place and for each country where the supplier holds inventory (both hard and soft). Tax processing functionality needs to be capable of evaluating the availability of consumption tax relief in the country of origin and applying consumption taxes in the country of destination.</p>	<p>Availability of multi-country tax tables of this kind? There are providers who have developed tax calculation tables principally for US state and local taxes and some countries outside. However, we are not aware of any provider with this level of capability at present. There is also the question of how these tables would be maintained and how emerging e-commerce products should be classified for the purposes of the multiple taxing jurisdictions involved.</p>
<p><b>Real-time validation</b></p> <p>As consumption taxes have a direct bearing on the price paid by the customer, it is necessary for taxing decisions to be made before payment is effected. This means that any validity check a supplier is required (by the tax authorities) to carry out in connection with customer-provided data has to be performed on a real time basis. <b>For on-line transactions with consumers, there is no scope to revisit the price at which the transaction was concluded.</b></p>	<p>Currently, there is no real time on-line facility for verifying customer-provided tax identification numbers. Service levels for systems such as VIES vary by country and would need to be hosted in an on-line environment, capable of handling significant volumes of "hits" if a real time verification process is to be enabled.</p> <p>Similarly, any mechanism for verifying customer-provided residency details would need to be a real time system capable of supporting the anticipated transaction volume demands.</p>

**Table 1 (continued).** Critical success factors

Requirement	Issue
<b>Tax inclusive settlements</b>	
The supplier tax processing system will have to make decisions that ultimately drive the price paid by the customer.	How will any conflicts between customer-provided information and the verification process be resolved during transaction processing?
<b>Multi-country invoicing capability</b>	
The supplier system will need to be capable of generating tax invoices where required by the relevant tax authority.	Variations in invoice content by country/local language/currency obligations.
<b>Multi-country record-keeping</b>	
Suppliers will need to be able to maintain accounting records to the satisfaction of the national tax authority concerned and implement processes to enable the filing and payment of taxes.	Scale of task/availability of local expertise.

*Additional observations*

26. The notion of using certificates of some type for B2B trade is helpful in creating certainty for the supplier in making tax decisions. The business members believe, however, that it may be helpful to point out that new developments in inter-company purchasing activity may make such an approach obsolete. Increasingly, businesses are decentralising their purchasing activity and allowing increasing numbers of employees to acquire goods and services directly from the supplier without involving the corporate accounts payable department. In such a case the use of certificates is less likely to be helpful. In fact, experience suggests that in such transactions it can be difficult to obtain the corporate customer's consumption tax identification number ("tax ID number"). One possibility would be to rely on the due diligence process in which customer and vendor master files are created in Enterprise Resource Planning (ERP) systems and leverage off that process to establish the tax status of customers and suppliers.

27. Alternatively, providing a system whereby merchants (or at least authorised merchants) could query a database to determinate and/or verify the tax ID number might help address this problem. At a minimum, a seller who is not able to obtain the customer's tax ID number should be able to charge consumption tax under the applicable rules without negative consequences. In such a case, the purchaser should have the right to offset the consumption tax in the normal course of the return filing process.

28. We would like to comment further on the use of thresholds to effectively address this issue. The first point that we would like to make about thresholds is that in devising a threshold, it is important to clearly identify the objective of the threshold and then to design it so that it has a reasonable chance of meeting the objective. The fundamental issue with thresholds is that they focus on revenue, whereas from a supplier perspective, the contribution of revenue to gross profit can vary widely from industry to industry. It is important that thresholds not be used in such a way that ultimately no taxation takes place.

29. We agree with the conclusion that the use of a fiscal representative (FR) increases the cost of compliance to suppliers (and thus may actually deter compliance). Further, the requirement to use a FR does not create any incentive to comply.

30. From a business perspective, the FR concept does not make sense. The model is typically based on the fact that the FR incurs at least a secondary liability to the local government in the case that the supplier has failed to remit the appropriate amount of consumption tax. The fees charged by the FR typically reflect the cost of assuming this potential liability. In the FR model, however, despite the increased cost to the supplier, the supplier continues to retain the primary liability and remains contractually liable to the FR even after the FR has discharged the liability to the government. The FR model thus results in increased costs from which only the government benefits as it now has two, rather than one potential point of recourse. The supplier receives little benefit from the much higher rates paid to the FR as the supplier continues to remain contractually liable to the FR (if not the government) not only for his own actions, but also for those of the FR.

31. From the standpoint of the FR, there is little incentive to provide these services, as the risk remains relatively high. It is difficult to establish appropriate fees and the fees are likely to be high compared with the cost of fulfilment of the associated administrative tasks. It is increasingly difficult for businesses to identify appropriate FRs in a number of jurisdictions.

32. The FR model might be more viable if the supplier and the FR are free to establish contractually the extent of each party's share of the overall liability. One drawback that remains with the FR model is that this solution does not scale for suppliers making supplies in a large number of jurisdictions.

33. The use of financial security statements or the posting of bonds may be difficult and costly for small and medium-sized enterprises (SMEs).

34. Although we agree that trusted third parties (TTPs) and digital certificates may be available at some stage to assist with tax compliance, we would caution governments from assuming that digital signatures and certification processes will be a de facto element of e-commerce. It is possible that low value transactions may continue to be offered until such time as the costs associated with digital certificates lessens significantly.

35. Under "Motives for Compliance" it is important to stress again that simplified consumption tax rules and a manageable compliance burden are extremely significant in motivating companies to comply with registration requirements. The existing level of complexity may make it unrealistic to expect high levels of non-local supplier compliance with a seller registration model (particularly in the case of SMEs). If the cost of compliance is high, businesses may weigh the risk of non-compliance against the cost of compliance and make a decision based on the perceived relative cost.

#### *Discussion of possible registration-based compliance model*

36. We think it is helpful to bring recent US state and local sales taxes developments to the attention of the OECD. A number of states are actively pursuing a possible solution to address the complex legal and constitutional issues regarding the requirement of remote sellers to register to collect and remit sales taxes. It is based on a substantial simplification of tax bases and the establishment of a single tax rate per state. To further simplify compliance the states hope to ultimately certify companies ("on-line tax processors") that would calculate, collect, and remit the tax to the local government. Suppliers that used these on-line tax processors for a given jurisdiction would generally have very limited audit exposure due to the reliance on a state certified vendor. (Detailed audits would apply only in cases of suspected fraud.) Supplier use of

the on-line tax processors would be voluntary, although the benefit of the simplification would be widespread. Large companies could still internalise this function and use existing tax computational software.

37. These developments are outlined in an article by David Hardesty published in *Tax Planning International's E-commerce*.<sup>3</sup> That article outlines the model as follows:

- The buyer enters personal and credit card information into the seller's shopping cart.
- Information is transmitted to the on-line tax processor to calculate tax. Information includes buyer location, buyer status (*e.g.* exempt or non-exempt), product code and price.
- The tax processor returns the calculated tax due, prior to the customer's completion of the purchase.
- The seller maintains credit card and other necessary information until the product is shipped. Upon shipment, the credit card is charged for the sale.
- Included in the credit card amount is the tax due on the sale. The tax is credited to the account of the on-line tax processor, not the seller.
- The on-line tax processor remits the tax and any other necessary information to state and local tax authorities.
- The on-line tax processor prepares tax reports for the seller.<sup>4</sup>

38. Given that most consumption tax regimes are considerably simpler than the current US sales and use tax system (*i.e.* fewer rates, fewer sub-national taxing jurisdictions), it might be worthwhile for governments to review this approach in greater detail. This type of approach offers a way to encouraging non-local suppliers to register for local consumption taxes while still providing local tax authorities with a source of reliable information. The TTP approach could significantly reduce the burden of compliance – particularly for SMEs as long as it is available at low or no cost.

39. Governments should consider the option of, in addition to certifying TTPs for local tax collection, whether it would be worthwhile to partially fund the cost of TTP services to increase compliance. Government could pay the costs for SMEs, or partially subsidise the cost.

40. It is important to note an important distinction between the TTP model suggested above and the existing FR concept. Under the TTP model, there is an effective transfer of liability from the supplier to the TTP once the appropriate information is provided.

41. There are however a number of issues with the approach identified above which must be considered in exploring how such a model might be utilised in an international context.

- 1) The TTP solution does not address invoicing. Existing requirements for invoicing are onerous in many countries and are not compatible with e-commerce. One possible solution would be to substitute a transaction number (provided by the TTP) which could be referenced by customers, suppliers and governments to verify the consumption tax charged on the reported transactions.

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3. Hardesty, David (2000) "United States Sales Tax and E-Commerce—Part II," *Tax Planning International E-commerce*, pp. 11-13, June.

4. *Ibid*, p 12.

- 2) It is questionable whether such a model is economically viable if the transaction base is limited to digitally delivered goods and services in B2C transactions.
- 3) We would suggest that the system be optional—at least in the near term. Larger more sophisticated taxpayers with advanced taxation systems on ERP systems have already made significant investments in tax compliance software and should be free to continue to use them if they prefer.
- 4) Whether TTPs offer a cost-effective solution for SMEs is another issue associated with the TTP approach. (The cost should be low enough so that an SME views it as a reasonable charge to eliminate or significantly reduce the risk associated with lack of compliance which is often due to a lack of understanding of the various local rules and requirements.) Much of the tax software available today requires costly set-up and customisation to accommodate different tax profiles. Simplification of consumption tax rules would help reduce the cost of this option.
- 5) Another way to reduce the cost of the option is to expand the scope of the TTP services to cover the shipment of physical goods. Services are being devised to calculate fully landed costs so that suppliers and consumers will know a transaction's full cost. If it were also possible for a TTP to remit the tax and duty and pre-clear the goods, border delays could potentially be eliminated. If a TTP provided services to both physical and digital supplies, it is possible that high transaction volumes would reduce prices for the service. (Note: If this method became common it may also be possible for governments to eliminate the duties and tax exemption for low value shipments.)
- 6) A final important point is that significant simplification of consumption tax rules is necessary for TTP models to work effectively. Under existing rules, the high level of complexity frequently requires an element of human intervention to make judgements where multiple treatments are possible. The need for human evaluation of transactions could make a TTP solution unworkable.

### ***Tax at source and transfer***

42. As presented in the WP9 Sub-group Paper, the tax at source and transfer would entail a high level of international co-operation, thereby making it unrealistic in the near term and difficult to achieve in the long term. The level of international co-operation may not be so high, however, when compared to the high level of international co-operation that is likely to be required to establish an enforceable supplier registration model.

### ***Additional points***

43. The most significant limitation of this discussion is that it is relatively narrowly focused on the way in which this type of approach might work and thus, it might be prematurely concluded that there is little potential here. For example, the approach assumes that governments would collect from local suppliers. This would not necessarily have to be the case. The suppliers could make remittances directly to the appropriate governments and provide proof of payment to the local country government.

44. We believe that the potential compliance burden for governments might be overstated. While the supplier's local government has the largest overall burden, the combined government investment in the one-time per supplier verification and enforcement process would be less when compared to the present recurring, multiple jurisdiction audit situation. In addition, the paper does not address the significant reduction in compliance burden that this option offers to business.

45. If a robust TTP industry developed, international co-operation might be limited to co-operation on the certification of TTPs to perform functions to collect and remit taxes to the various jurisdictions. Agreeing to co-operate in this manner, including an agreement that participating jurisdictions would require suppliers to use certified TTPs or provide data on international transactions for information sharing could be sufficient.

#### ***Withholding by payment solution providers***

46. In response to the publication of the Technology TAG Paper, a number of financial services companies—particularly credit card companies have submitted papers to the OECD to express a number of significant issues and concerns. We welcome this information and to the extent points discussed below are contrary to points made in those submissions, we would defer to their papers.

47. We agree with the Technology TAG Paper’s conclusion that the suggested framework is unrealistic.

#### ***Additional points***

48. It is important to note that the problem of determining the jurisdiction of the taxpayer is as much of a problem in the seller registration model. This problem needs to be addressed in all the models discussed with the exception of the self-assessment model.

49. We disagree with the contention of some observers (as reported in the WP9 Sub-group Paper) that tax collection mechanisms that target either the supplier or recipient “will ultimately fail to collect more than a fraction of electronic commerce transactions.” We feel this statement is based primarily on the status of existing tax systems, inaccurate perceptions of the desire of business to comply with tax laws, and that the development of the technological infrastructure that will ultimately support e-commerce is still in very early stages.

50. The suggestion that the “Withholding by Payment Solution Providers” approach is the only solution that will require investment in the development of new collection mechanisms is not correct. Any collection mechanism to deal with e-commerce will require significant investment by both business and government.

51. We are concerned that the Paper indicates that a review and revision of consumption tax laws is only necessary under this option. We believe that dramatic simplification of existing consumption tax laws will be necessary for the success of any type of collection approach. For example, any option that involves a TTP, will be far more successful far earlier if simplifications occurred which made it possible for a TTP to provide services other than simply the computation of applicable taxes.

52. Payment providers or credit card companies do not provide suitable information that can be used to determine the jurisdiction of consumption at the present time. The credit card company papers provide further information about the nature of information available in accounted payment systems and why it is not suitable for this purpose. In the near term, suppliers should be permitted (but not required) to use customer provided credit card billing addresses to determine the jurisdiction of consumption, if the supplier believes it provides a more reliable indication than other available information. Suppliers should not be required to verify the address on-line because it is frequently not possible or practical. In situations when the billing address cannot be verified on-line, the supplier should not be required to verify the billing address “after the fact.”

## An argument for allocating responsibilities for the collection of tax

53. The traditional supplier-based consumption tax compliance model was primarily based on the fact that the supplier had the necessary information to determine and collect the tax. This model also provided the government with a consolidated information base, simplifying enforcement efforts. The increase in cross-border trade suggests that significant changes must be made in the basic assumptions on which the supplier-based model relies. It may be helpful, therefore, to review the necessary tax collection elements and how these could be allocated in a cross-border situation. See Table 2 below.

**Table 2.** Allocating responsibilities for the collection of tax

	Supplier	Consumer	Payment Solution Providers and other enablers
<b>Attribute</b>			
Consolidation	The general premise that it is easier to enforce compliance with fewer sellers rather than a large number of consumers becomes less true as cross-border trade increases. The number of suppliers will also increase.	The large number of consumers suggests that little leverage is obtained using a consumer-based collection mechanism absent any leverage provided by other transaction parties.	Payment solution providers (PSPs) and other enablers potentially offer the highest degree of consolidation in a cross-border environment as there will generally be fewer enablers than suppliers.
Availability of funds	Suppliers received funds from the consumer and thus could also collect tax from the consumer. In a cross-border environment suppliers will continue to collect funds.	The consumer has the funds to complete the transaction and potentially could make the tax payment at the time of purchase. (We agree that collection of tax after the transaction reduces the likelihood of collection.)	The PSPs using their expertise in funds settlement could divert the payment of tax directly to the tax authorities provided that they had sufficient information regarding the amount of tax to be remitted.
Availability of tax decision-making information	In a cross-border environment the supplier is much less likely to have valid and verifiable information about the tax residence or status of the consumer. A supplier may have information about the tax rules and rates, particularly in markets in which final consumer price points are a concern. It would be helpful if governments made clear and unambiguous information about local tax rules readily available.	In a cross-border environment the consumer may be the only party that fully understands his tax status. The consumer is not likely to have adequate information to determine tax liability.	It is unlikely that the PSPs would have sufficient information about the transaction, the consumer, or the supplier to make an accurate tax determination.
Jurisdiction to enforce compliance	In a cross-border environment, under current legislation, governments do not have much jurisdiction over non-local suppliers.	Governments likely will continue to have jurisdiction over consumers.	Governments are not likely to have jurisdiction over the merchant bank. It is possible there might be some jurisdiction over the consumer's bank. Governments probably may not have jurisdiction over PSPs.
Incentive to Comply	Legitimate business will comply as long as the cost of compliance is lower than the potential exposure that arises from non-compliance.	Consumers will have little incentive to comply as long as the perceived risk of non-compliance is relatively low	PSPs will probably have the greatest incentive to comply if scale reduces the impact of compliance costs. In other words, PSPs might be able to leverage the cost of compliance over the largest volume of transactions.

54. Based on the analysis above, it becomes clear that centralising the entire responsibility for tax rate determination, tax collection, and compliance with the supplier becomes less viable where high levels of cross-border trade are present.

55. Given the impact of the increase in cross-border trade, particularly through e-commerce technologies, it is useful to reassess the fundamental principles upon which current consumption tax systems are based.

- 1) Does it continue to make sense to make a single party bear the complete responsibility for compliance with the consumption tax system?
- 2) Would it be possible or feasible to imagine that various parties to the transaction could assume responsibility for different aspects of consumption tax compliance resulting in a more realistic burden for each party, without reducing the robustness of the enforcement tools available to governments?

56. This paper includes considerable discussion of the potential role of TTPs. That focus is due to our observations that new indirect tax application companies (ITACs) are being established to develop business solutions to cross-border e-commerce tax issues. These ITACs are at various stages of development at the present time. One of their biggest challenges is incorporating the human analysis that is presently required to make some tax decisions.

57. In most cases, the solution focuses primarily on the computation of the correct tax. We have suggested that it may be possible for these ITACs to perform a larger role if there was market demand. In the example above, it is suggested that TTP reporting to governments and customers could ultimately replace the need for formal tax invoices and the preparation of consumption tax returns by suppliers.

58. In addition, we have suggested that the tax collected could be remitted directly to the appropriate governments. This would entail the co-operation of the PSPs, which would require further analysis. It is important to stress that we do not propose that the PSPs assume any responsibility for the determination of the tax. Their liability should be limited to ensuring that any tax collected is remitted directly to the government unless the supplier is remitting the tax.

59. Governments too have an important roll to play. If these ITACs are to provide a total solution, it is important that governments work with them to determine how information provided by the supplier to the TTP might be used. Some ideas include providing substitutes for formal tax invoices as an audit trail, or even the preparation of consumption tax returns. The more governments learn about and follow the development of these ITACs, the more prepared they will be to leverage the services they want to provide. The reduction of costs to suppliers and their own administrations is just one likely result.

60. Further, it is important that governments make critical decisions about how they wish to enforce consumption tax compliance. It is vital to realise that it is highly unlikely that technological advances will ever provide a total solution to the question of enforcement. Governments must decide whether they would prefer to retain local control of enforcement with a view to creating a consumer based enforcement mechanism or whether they prefer to expand levels of international co-operation to enforce non-local supplier compliance.

## Suggestions for the near term

61. In the near term, revenue losses or border tax collection issues relating to e-commerce transactions are likely to be limited. This is especially true for B2C e-commerce transactions. Businesses in jurisdictions where consumption tax is required to be charged are legitimately concerned about the competitive disadvantage that could arise where they are obliged to add consumption tax to their supplies while non-local suppliers can digitally deliverable supplies without collecting tax. In jurisdictions with high rates of consumption tax the resulting price differential can be significant enough to alter consumer behaviour.

62. Jurisdictions wishing to foster an environment that encourages local e-commerce to grow and flourish should recognise this issue and consider whether or not it makes sense to devise near term solutions to address the problem. Without further developments in technology or the creation of international mechanisms (which will take time), options are limited.

63. One option is to require non-local sellers to register and collect tax. To be successful, it is important that governments realise that the best way to encourage compliance with seller-based registration models is to make consumption tax registration as easy as possible, to keep consumption tax rules simple and straightforward, and to make a commitment to reduce the potential for double taxation. It is important to note that the approaches, which can be put into place in the short term, are very limited.

64. The greatest concern of governments in the near term appears to be enforcement of a non-local supplier registration regime. In this regard, we would offer the following suggestions for your consideration.

- 1) Keeping the costs of compliance for suppliers as low as possible and establishing “realistic” thresholds for registration, will help minimise the impact that the cost of compliance has on making a decision to comply. For example, if it costs French francs (FRF) 10 000 a year to maintain a French consumption tax registration, a supplier may choose not to comply unless the amount of French consumption tax due exceeds that amount.
- 2) It might be appropriate to impose penalties for the failure to collect, remit and report consumption taxes that are due on supplies made by non-local suppliers. Although it might be difficult to collect penalties from non-local suppliers, those who ultimately plan to set up local operations will consider the exposure to tax and penalties due a significant risk.
- 3) Another option to consider is whether it makes sense for the consumer to be liable for taxes that the supplier fails to collect. Although under current tax systems it is not likely that many consumers would voluntarily remit taxes due, it might discourage some consumers from acquiring digital goods and services from non-registered suppliers.
- 4) One recommendation is to direct the focus of government enforcement efforts towards suppliers that do not appear to be making any attempt to comply, rather than on suppliers that are registered and that complete regular tax return filings.
- 5) In some cases it may be possible that the supplier is making both physical and digital supplies. If this is the case, the customs authority is likely to have additional information about the supplier from shipping documents.

65. In conclusion, we can not stress enough that **the easier and less costly it is to comply, the greater the level of compliance.**

**ANNEX IV:  
PAPER ON CONSUMPTION TAX-RELATED BARRIERS**

**A BRIEF SUMMARY OF SOME CURRENT CONSUMPTION TAX BARRIERS TO  
ELECTRONIC COMMERCE (OCTOBER 1999)**

1. The Government members of the Consumption Tax TAG note that in the existing consumption tax systems there are aspects that are perceived by the business sector as barriers to the execution and growth of electronic commerce. The members recognise that some of these aspects perceived as barriers involve politically sensitive issues and that some of them need some time to be examined and cannot be changed in a short period of time.

2. The business members of the Consumption Tax TAG note that substantial barriers to the execution and growth of electronic commerce are present in existing consumption tax systems. In reassessing how consumption taxes might be effectively applied in an e-commerce environment and also how compliance might be enforced given the cross border nature of the trade, the business members felt that it would be useful to highlight existing trouble spots. By doing so, they feel that they are less likely to suggest approaches for e-commerce which might result in similar issues. In addition, it may be possible for certain issues to be dealt with for the benefit of conventional trade.

3. The business members appreciate that some of the complexities may be difficult to eliminate in the near term, and the primary purpose of this paper is not to function as a list of suggestions for immediate improvement. Instead we hope that this discussion of difficulties helps tax authorities appreciate the types of things that are complex since this is not always apparent. As businesses move to increasingly computerised enterprise platforms, many tasks that were managed manually in the past now need to be adapted to work in a computerised environment. Compliance requirements, which were simply time consuming in the past, are increasingly becoming tasks that are nearly impossible to manage in a computerised environment and will not be manageable given the time constraints surrounding an electronic transaction. In conclusion, we hope this paper provides useful information to tax authorities so that they have a better idea of the current difficulties and where those difficulties are likely to result in the inability of businesses to comply with tax rules.

4. These difficulties fall under the following headings, each of which will be discussed in turn.

- A. Liability issues.
- B. Rates of tax.
- C. Administrative issues.
- D. Practical issues.

## A. Liability issues

5. In view of the broad span of different consumption tax systems which exist across the world, a number of problems and potential barriers arise:

- (i) **Complexity** – consumption tax systems are too complex and require too much analysis. In order for a supplier, purchaser or tax authority to work out the tax liability of a sale detailed information needs to be collected. For example:
  - How is the product categorised? This is a particularly difficult question as most existing tax regimes never contemplated the types of supplies that might be available through e-commerce and other technological developments. For example, it is now possible to download from the Internet pictures, photographs, maps etc for one-off use by the purchaser and with no potential for commercial exploitation by him. Should this fall under consumption tax rules regarding the right to use intellectual property? Or, should the transaction be more appropriately viewed as a transfer of copyrighted articles which historically have been treated as supplies of goods, or are they a more ephemeral purchase which needs a formulation of new rules?
  - What is the status of the customer? (*i.e.* taxable, non-taxable, exempt)
  - What is the supplier's business structure and where will the tax authorities see the transaction taking place? The supplier's structure is relevant so as to know in which country the transaction takes place. For example, if a bank is structured to have branches all over the world and offers on-line banking, it is possible that the customer may have a banking relationship with his local branch, but that the on-line banking service may be provided from a centralised hub in another country. The tax rules need to define which part of the entity should be treated as providing the on-line service to the customer.
  - On what date will the tax authorities regard the transaction as having taken place?
  - How will the product be used? This question is particularly relevant in the system of sales and use taxation applied by many of the states in the United States. Purchases for resale, use in manufacturing, and use in research and development are sometimes exempt from tax and sellers can be required to maintain evidence, supplied by the buyer, of exempt use.
  - The Consumption Tax TAG understands that in its studies on VAT and the Single Market the European Commission has itself identified that large numbers of data – possibly as many as 26 or 27 – may be needed to work out the VAT liability of a sale. This would be an impossible burden in a fast-moving e-commerce environment. (See Annex A for examples of data requirements.)
  - Finally the Consumption Tax TAG believes that it is important that businesses should not have to “reinvent the wheel” in working out their tax positions when doing business in a new way or in a new country.
- (ii) On top of the detailed information required, *other legal and administrative issues* may prevent collection of the data and proper analysis. In constructing taxation systems, cognisance should be given to relevant privacy rules. Governments will need to discuss the interaction of privacy laws with tax compliance requirements and also consider the global dimension of potential conflicts.
- (iii) A particular problem faced by suppliers is *conflicting national legislation, interpretations or administrative rulings given by different authorities* to define commonly used terms that define taxable and exempt product categories. Where conflicting interpretations arise this can of course lead to either double taxation or non-taxation.

- An example of conflicting national legislation is the use of Sixth VAT Directive principles by non-EU countries. For instance, some non-EU countries use the principles of Article 9(2)(e) of the Directive. However, their interpretation of place of consumption is different. As a result, banking and insurance businesses are confronted with double taxation.
  - Furthermore, some non-EU countries apply a different kind of reverse charge mechanism. Taxable persons are not entitled to credit the VAT which they are due as a result of the reverse charge mechanism.
  - An example of conflicting interpretations or administrative rulings in the electronic commerce arena is the concept of “on-line diagnostics”, an increasing business trend, whereby, instead of sending personnel to physically mend a customer’s computer or server etc, the problem can be diagnosed by messaging between the supplier’s systems and the customer’s equipment, and can be subsequently resolved “on-line” without the need for human intervention. The Consumption Tax TAG notes that tax administrators around Europe may have given inconsistent rulings on the tax treatment of this type of service. Some say that it equates to physical work on goods and is thus subject to VAT in the country where the customer’s equipment is situated. Others would accept that this is consultancy or data processing and thus taxed differently.
  - Some jurisdictions might also define the tax base or taxable amount differently. For example, freight, postage, or handling charges can be included in the taxable value or tax exempt. The time of taxation can also vary significantly depending upon how a product is characterised.
  - Another area where differing practices create potential barriers are “bundled” supplies. No clear common rules exist to determine whether VAT should be charged on separate elements of the transaction or to the product as a whole. In others, the position is left open for the courts to decide on a case by case basis. This latter stance has recently been endorsed by the European Court of Justice in the Card Protection Plan case. On-line vendors of “bundled” services are not thus able to identify a single rule that works for all their sales around Europe. More examples will emerge as e-commerce develops.
- (iv) *Substantial simplification* of consumption tax rules, including international co-operation and consistency, is required so that e-commerce can flourish.

## **B. Rates of tax**

- (i) The *wide range of rates* in existence (varying from 0% to 33% around the world for example) combined with *differing interpretations* of what falls into the various rate categories, makes it very difficult for sellers to correctly account for their liabilities. Simplification and harmonisation of rates would lead to better compliance both with regard to traditional commerce as well as electronic commerce.
- (ii) The Consumption Tax TAG notes that *different consumption tax rates may be applicable to hard and “on-line” versions of the same product*. Books and newspapers are the clearest example of this situation. Business believes that the charging of different consumption tax rates to similar products will act as a serious barrier to the growth of electronic commerce.
- (iii) The variation in rates – combined with requirements to publish prices inclusive of tax – presents a *problem with on-line quotation of prices*. It can be anti-competitive to publish different prices for different countries, even if the difference is only due to VAT rates. Order processing and billing

system requirements and costs are increased because these systems must be able to meet local requirements that can be inconsistent, complex, and contradictory.

### C. Administrative issues

- (i) The Consumption Tax TAG notes that *simplicity of administration* helps both business and tax authorities in that it leads to a more efficient tax collection and audit process. *Particular problems* noted in this area are:
  - The requirements of notification, registration and reporting obligations vary enormously around the world. The Consumption Tax TAG believes that it is impossible for even large businesses to fully understand and comply with its obligations in these circumstances. It is, of course, even more difficult for small and medium enterprises to try and cope with these multiple obligations.
  - The burden of multiple different registration and reporting obligations is likely to be exacerbated by the growth in use of Enterprise Resource Planning (ERP) systems such as SAP, Peoplesoft and Oracle. These are computer systems which enable companies to have a global view at any one time of their inventories/sales and debtors and to effect real time sales and purchases. These systems can be used to streamline tax reporting but the systems adjustments needed are expensive and time-consuming. Furthermore, businesses seek to use these systems to rationalise their accounting procedures and to achieve efficiencies and cost savings. However, an important part of the streamlining process may involve raising invoices at a central point. Tax administrations should recognise these changed methods of accounting and bookkeeping.
  - Given the complexity of obligations referred to above this may be difficult to achieve with full compliance and may leave the supplier with an audit risk. In particular, suppliers want to be able to have complete flexibility in sourcing and shipping goods to customers: this is needed to minimise costs/maximise efficiency. Under current consumption tax rules, changes of liability can be caused by a basic business decision concerning the source of goods to fulfil an order. Complexity of tax systems should not be a barrier to efficient sourcing of goods.
  - ERP systems are very relevant to e-commerce as the next generation of this type of software is being developed on a web-based technology that enables the ERP systems of suppliers and purchasers to “talk” to one another without human intervention. Sourcing of product/sales decisions will therefore be even more business-driven, with difficulties if this does not work well in the framework of tax rules.
- (ii) The Consumption Tax TAG notes that *cross-border reclaim procedures*, such as the EC 8<sup>th</sup> and 13<sup>th</sup> Directives may be a possible or partial answer to the problem of double taxation, provided such procedures are simple to operate and provided that refunds are paid on a timely basis. These reclaims involve the payer of VAT making a simplified reclaim for repayment direct to the VAT office of a government with no need for VAT registration or taking a VAT number.
- (iii) “Reverse charge” procedures sometimes help to alleviate the problems otherwise associated with imposition of complex consumption tax determinations upon non-residents.
- (iv) It is also extremely difficult and costly to comply with *requirements to maintain systems or copies of invoices locally*.

## D. Practical Issues

- (i) Business notes that there are *practical issues that need to be addressed* in order to make *VAT reporting and accounting for e-commerce as smooth as possible*. Some examples of these are:
- Where VAT numbers need to be provided as evidence of customer status, some method of instantaneous verification needs to be available for on-line suppliers or else transaction processing will be aborted or slowed down. Alternatively non-resident sellers should not be held accountable where a customer provides an incorrect VAT number.
  - Governments should consider relaxing restrictions on the display of prices on an inclusive of tax basis. Until the seller has obtained sufficient information from the customer, there is no way that a tax-inclusive price can be offered. Rules on the content of advertisements, catalogues and invoices should allow prices to be quoted without VAT, providing it is clear that VAT will be charged on top.
  - It is often unclear how to apply VAT when the purchaser is a self-employed person (and might have mixed business/personal use) or where a private customer is shopping on-line from an office PC. The Consumption Tax TAG would advocate a practical workable solution e.g. assume that business use is intended where a VAT number is proffered.
  - If the OECD, its members, or another country decides to require some form of “remote” registration for non-resident suppliers, considerable simplification of consumption tax registration requirements around the world is urgently needed.
  - In addition, substantial simplification and harmonisation of record-keeping and invoicing requirements is needed. Examples of some of the problems are:
    - prohibitions on the use of electronic invoicing
    - requirements for a foreign supplier to store paper copies of invoices in the country of registration
    - different formats for official VAT invoices
    - language requirements, if the language of the transaction should be the language used for the invoice
    - obligations to keep a specific sequence of invoice numbers for the country of registration even though this cannot be integrated with the suppliers general accounting system and serves no commercial benefit.
  - Working to simplify all of the above matters and adopting a practical simple tax system should benefit both conventional and e-commerce. The Consumption Tax TAG notes that it may be possible to harness technology in order to improve audit by tax authorities and so simplify these currently complex requirements.

### Draft conclusion

6. The Consumption Tax TAG is of the opinion that there are substantial current barriers in consumption tax systems to the growth of e-commerce, as outlined above. The OECD process for reviewing the rules should be taken by the tax authorities, working in conjunction with business, as an opportunity to address these barriers, so that both conventional and e-commerce can flourish.

## Annex A

### FACTORS DETERMINING THE INVOICING AND TAXING DECISION

1. Is the supply that of a good or service?
2. Is the supply a “bundle” of goods and services?
3. Is the supply entitled to or subject to a rate of tax other than the standard rate?
4. Is the supply a bundle of goods/service (or both subject to different rates)?
5. Is the customer taxable (VAT registered)?
6. Can I rely on the VAT number provided by the customer to assume that the customer is registered (*i.e.* does it even look right)?
7. Where do I ship the goods or supply the service?
8. Is the customer receiving the goods outside of his country of establishment and if so where?
9. Where am I making the supply from and will the sending and receiving country agree this is the same place.?
10. What is the currency of the transaction and will I need to convert that currency into a different currency for purposes of issuing a VAT invoice?
11. Do I need to worry about where the customer is “using and enjoying” the goods or services in order to decide which country’s VAT is due.
12. If the answer to 11 is yes, have I exceeded the Distance Selling thresholds so that I need to charge VAT at the location of the consumer?
13. On cross boarder sales am I able to determine whether my non-registered customers are individuals (distance selling rules) or non-registered businesses (subject to local VAT/acquisition VAT depending on amounts involved (*i.e.* can my computer system recognise and treat John Doe as a consumer and Joe Doe’s unregistered business as a non-registered business?).

**ANNEX V:  
PAPER ON SIMPLIFIED INTERIM APPROACH**

*[Outline of the Consumption Tax TAG Business Members' Recommendations for a Simplified Interim Approach, as submitted to the WP9 Sub-group on Electronic Commerce, November 2000]*

1. The business members of the Consumption Tax TAG are concerned that existing consumption tax systems could create a significant impediment to the development of e-commerce both within domestic markets and in the global market place. As most consumption tax systems were designed some years ago, current systems are not capable of dealing with the issues which arise from the development of e-commerce. For governments, the primary concern with consumption tax and e-commerce relates to business-to-consumer (B2C) transactions that involve digitally-delivered services and intangible goods.
2. For most services, the place of supply is defined currently as where the supplier is established. This general rule creates an un-level playing field because non-resident suppliers can sell into local markets without charging the applicable consumption tax of the local jurisdiction, thereby placing local suppliers at a competitive disadvantage. The Ottawa Framework Conditions (the "Framework") recognised this issue and provides a set of recommendations to address it. The business members endorse the Framework; however, it fails to provide a means of implementing these conditions. The business members suggest that the Simplified Interim Approach (SIA) be adopted as a means of implementing the Framework in the near term.
3. Other key concerns that business members have with respect to the application of existing consumption tax systems to on-line B2C transactions include:
  - The development of e-commerce technologies may result in the ability to complete an entire transaction on-line including the delivery of an electronic invoice. The current requirement in many countries to produce and issue paper invoices is likely to limit the ability of vendors to engage in low value transactions.
  - An on-line transaction requires the determination, using automated systems, of the appropriate jurisdiction and rate of tax at the time of the transaction. The complexity present in many systems, however, requires an element of human judgement that currently cannot be imported into automated tax calculation systems that are required to calculate tax at the time of the transaction.
  - In an on-line transaction, businesses currently are unable to verify user-provided information against external data sources because such data is unavailable or cannot be accessed instantaneously.
  - The present lack of standardisation in registration and compliance procedures makes compliance a manual—and therefore cumbersome—process. This frustrates the development of systems-based solutions.
4. In recognition of the wide acceptance of the principles agreed to in the Framework, the issues identified above, and the current limitations of technology to provide more robust technical methods to collect consumption taxes, the business members of the Consumption Tax TAG have determined that the most viable means of providing for the collection of consumption taxes at the place of consumption currently is a simplified approach to the supplier-registration model—the SIA.

5. The SIA is predicated on the following assumptions:

- In the near term, the amount of consumption taxes arising from B2C transactions that involve digitally-delivered intangible goods and services is relatively low.
- The need to create a level playing field for local vendors is perhaps more important, in a number of jurisdictions, than the actual potential for revenue leakage (at least in the near term).
- In the near term, most supplies of intangible goods and services on a cross-border basis are likely to be made by larger and more sophisticated companies who are capable of dealing with at least some of the complexities of cross-border trade.
- Larger companies are better equipped and more inclined to be tax compliant for a number of reasons—corporate image, operations in a large number of countries, etc.
- The fact that most consumption taxes, if properly determined and remitted, do not represent a cost to the company creates an automatic incentive for compliance when the cost of compliance is not excessive and when there are perceived negative consequences associated with non-compliance.

6. In the near term, in the absence of more robust agreements for international co-operation in the administration and enforcement of consumption taxes, simplification remains the tax authorities' single greatest tool to encourage compliance. **The easier and less costly it is to comply, the greater the level of compliance.**

7. It is important to note that we are not advocating optional compliance in the SIA. We believe it would be appropriate for tax authorities to impose penalties for wilful non-compliance. We would also like to add that companies that make a real effort to comply with consumption tax requirements should be respected for doing so and should not be subject to penalties or additional tax collection obligations for "honest mistakes" or the inability to independently verify information provided by customers where there is no means of doing so. If penalties are imposed against companies that make significant efforts to comply, a signal is sent to other companies that compliance efforts may not be "worth" the cost or risk.

8. In devising the SIA we considered the following items associated with the consumption tax compliance process:

***1) Determining where the supplier is established***

At first glance, this determination may appear to be relatively straightforward. Complexity arises in an on-line environment, however, when a number of affiliated parties may be making supplies through a single global network. We suggest that the supplier is established where the legal entity engaging in the transaction has its primary place of business regardless of where the servers, routers, and other hardware used to make the supply are located.

***2) The location of the customer***

In the near term, it will be extremely difficult to obtain information regarding the customer's location that can be verified during the course of an on-line transaction. The supplier should be able to rely on the best information available at the time of the transaction to make the determination of applicable taxing jurisdiction. This information could include information provided by the customer, the language of the product, the market that was targeted in the offering, or any other information available to the supplier. It should be sufficient that a

supplier has made a reasonable effort to determine the location of the customer, and no penalty or additional tax liability should be imposed on the supplier.

### **3) *The status of the customer***

The supplier must determine whether the customer is a taxable entity subject to a reverse charge in which case the supply may be zero-rated. We applaud the announced intentions of certain jurisdictions to create tools to facilitate this process. Until such tools are available, however, the best efforts of the supplier to make such a determination should be respected.

### **4) *The nature of the supply***

Clear and simple rules should apply to all types of supplies that can be remotely fulfilled on-line. The existence of different rules for different types of supplies is likely to result in high levels of uncertainty. Especially in the near term, it is important to recognise that advances in technologies will create supplies that are extremely complex to categorise under existing rules. For example, a single supply could include elements of telecommunications services, cultural or educational content, and even some incidental form of physical media where bandwidth is insufficient to complete the entire supply.

Where multiple rules create uncertainty or the potential for double taxation, suppliers should be able to obtain binding guidance from tax authorities within a reasonable period of time as to the appropriate treatment. Furthermore, mechanisms need to be developed to deal with the potential for double taxation.

### **5) *Registration in appropriate jurisdictions***

Once a supplier has determined that an obligation exists to collect the tax of a particular jurisdiction, the supplier should be able to register in the jurisdiction electronically. As soon as possible after filing the registration form, the supplier should receive a tax identification number. Suppliers may reach new markets in an e-commerce environment without necessarily targeting them specifically, which could trigger requirements to register and collect tax without advance warning.

We suggest in the SIA that suppliers be permitted to register on-line, without the requirement to post a bond or appoint a local agent. The information required from the supplier in the registration process should be limited to only that information which is required by the tax authority to administer consumption taxes. We note that tax authorities frequently use consumption tax reporting to obtain information for other purposes. We suggest that tax authorities consider whether such information is truly required from remote suppliers. By limiting the information requested from suppliers, it is much more likely that global registration standards will emerge, further facilitating compliance, and in the future, even facilitating cross-border co-operation in administration and compliance.

All necessary information required to register and comply with the local consumption tax regime should be available free of charge via the Internet. Ideally, tax authorities could notify the corporate tax personnel by e-mail in the event of any changes in law or filing requirements. (In this regard, it might be useful to request e-mail contact as well as physical contact information in the registration form.)

All required forms should be available for download over the Internet. And, as soon as is feasible, arrangements should be made for the electronic filing of those forms.

The SIA registration and administration process removes much of the otherwise available controls over claims for the recovery of input tax. (However, future technologies may restore possible controls regarding the recovery of input tax.) The business members suggest that in return for the simplification of the filing requirements, it may be appropriate to eliminate the ability of non-local suppliers, who elect to use the SIA, to recover input tax. This implies that if a non-local supplier chooses to use the SIA, the non-local supplier cannot claim input tax. If the non-local supplier does not use the SIA (*i.e.* a normal tax return), however, the non-local supplier is entitled to claim input tax. (We would like to note, however, that simplification would also benefit suppliers engaged in conventional commerce and any simplification that does not impact the tax authorities ability to control the recovery of input tax should be made available to all taxpayers.)

#### **6) *Invoicing the customer***

In consumption tax systems the invoice is the critical control document that allows the system to function with relatively low levels of fraud or abuse. In the e-commerce environment, however, it is absolutely crucial that invoicing be as simple and cost effective as possible. In this regard, we would like to offer the following suggestions for consideration:

- i) Electronic invoicing should be permitted as soon as possible.
- ii) Until electronic invoicing is permitted, we suggest that invoices only be required to be produced upon specific request of the customer or in cases where invoices are required to support claims for the recovery of input tax. This implies, e.g., that invoices are not required for transactions with private consumers or for transactions that are subject to the zero rate as a cross-border supply (the reverse charge procedure would apply).
- iii) The data required on the invoice should be standardised as much as possible and should be limited to the data required by tax authorities to administer the consumption tax regime. It should be possible for the supplier to invoice in his own language.
- iv) Sequential invoicing rules should be flexible to permit multiple sequences for multiple consumption tax registrations and potentially multiple types of supplies that run through different programs.
- v) We suggest that whether or not a tax invoice is issued, the vendor should be required to retain the complete details of the transaction for a reasonable period of time so that the details can be provided either to the customer or the tax authority upon request.
- vi) A vendor should be able to indicate the amount of tax and the amount of the transaction in the currency of the transaction and indicate only the exchange rate used to convert those amounts into the local currency amounts reported on consumption tax returns.

[It is extremely difficult to obtain and use specified exchange rates from central banks on invoices as such information is not often available on-line in forms that can be effectively linked to invoicing systems. Since the only objective of stating the exchange rate is to ensure that any tax recovered by the customer is equal to the tax paid in by the supplier, it should suffice to simply indicate the exchange rate that the supplier is using.]

### **7) *Remitting the tax***

The supplier should be able to remit the tax due electronically using any widely tradable currency or local currency.

### **8) *Filing the return***

The business members recommend that returns be as simple as possible – that they be designed to collect only the information required to administer the consumption tax regime. It should be possible to file the return automatically and receive confirmation of receipt of the return automatically. (As indicated in Item 5 above regarding registration, the simplification of returns is likely to result in greater levels of standardisation that may increase simplification globally, therefore, generating greater cross-border co-operation.)

### **9) *Enforcement***

Tax authorities should focus the majority of their enforcement efforts on identifying and notifying suppliers that appear to have a registration requirement that is not met. Efforts to educate suppliers and simplify the means of compliance are likely to increase compliance much more effectively than subjecting compliant suppliers to costly audit procedures. The imposition of penalties on registered suppliers should be limited to only gross negligence or fraud – for example where tax is collected and not remitted.

Tax authorities should be entitled to request information from suppliers to develop an understanding of their compliance procedures. It might be more appropriate, however, to treat such situations as “mutual education procedures” where taxpayers and tax administrators can learn “best practices” from each other.

Any tax audits should be conducted on a timely basis. Taxpayers should be able to provide information in an electronic format.

9. We believe that the suggestions above will encourage compliance with consumption tax systems in the near term and that implementing a simplified approach in the near term will do much to facilitate the development of longer term solutions. Specifically, we see the following benefits of the SIA:

- Reduction of existing market distortions (a more level playing field).
- Generation of tax revenue (which could be invested in e-commerce solutions).
- Act as a trigger for the development and improvement of e-commerce tax solutions.
- Encourage the simplification of existing systems, which will facilitate the development of increasingly automated systems benefiting e-commerce and conventional commerce; and
- Result in some level of global standardisation, benefiting governments as they seek to develop structures for international co-operation in tax administration and enforcement.